ELECTRIC POWER TRANSMISSION EXPANSION PROJECT

(PN-0061)

EXECUTIVE SUMMARY

BORROWER AND: GUARANTOR:	Republic of Panama	
EXECUTING AGENCY:	Empresa de Transmisión Eléctrica S.A.	
AMOUNT AND SOURCE:	IDB/OC:	US$ 79 million
	Local counterpart funding:	US$ 35 million
	Total:	US$114 million
FINANCIAL TERMS AND CONDITIONS:	Amortization period:	20 years
	Disbursement period:	3 years
	Interest rate:	variable
	Inspection and supervision:	1%
	Credit fee:	0.75%
	Currency:	Single-Currency Facility in United States dollars

OBJECTIVES:

The overall objective of this project is to aid development of a safe and reliable transmission system, by financing essential investments in power transmission, the sole operating activity involving electric power that will remain in State hands. Development of an adequate transmission network is indispensable for achieving efficient operation of a competitive electricity market with participation by the private sector, as sought by the current reform.

The specific objective of the project is to increase capacity and improve the reliability of the main electric power transmission network from the western part of the country to the metropolitan area of Panama to facilitate the supply of power from the hydroelectric generating resources in Panama, especially the Guasquitas-Canjilones project and ones in Central America related to the project: Sistema de Interconexión Eléctrica para los Países de América Central (SIEPAC) [Electric System Interconnection for the Countries of Central America].

DESCRIPTION:

The project consists of (i) the construction of approximately 400 km of 230-kV dual-circuit transmission lines from the Guasquitas substation to the Veladero substation (90 km), from the Veladero substation to the Llano Sánchez substation (110 km) and from Llano Sánchez to the Panamá II substation (194 km); and (ii) construction of the new Guasquitas and Veladero switching substations in the province of Chiriquí and expansion of the Llano Sánchez transformation substation in the province of Coclé as well as the connection, control, and protective equipment associated with the transmission line in the Panamá II substation, which will be constructed at the same time.

ENVIRONMENTAL REVIEW:

The line will produce minor environmental and social impacts because most of the line area is sparsely inhabited and devoted mainly to stock raising and agriculture. The most important environmental impact will be the cutting of trees along the right of way of the line, which passes through 7.4 km of forest in the reverted area of the Panama Canal and in Camino de Cruces Park (a total of some 50 hectares of cutting). This inevitable impact will be kept to a minimum, as specified in the environmental management plan. The most important socioeconomic impact concerns the relocation of less than 90 dispersed dwellings ? there are no clusters ? and some 50 hectares of tree plantings in the right of way. The number of affected dwellings was minimized with the route that was chosen. There is no impact on indigenous communities. It will not be necessary to relocate any indigenous dwellings. The environmental management plan proposes adequate measures to prevent and mitigate environmental and social impacts.

BENEFITS:

In addition to making possible the transmission of energy from hydroelectric projects in western Panama, specifically an average 695 GWh per year of energy from the Guasquitas-Canjilones plant and, beginning in 2004, energy exchanges with the SIEPAC, the line will provide benefits through the reduction of losses and increased reliability of the Panamanian trunk line transmission system. In addition, the line will aid the development of a reliable and safe transmission system that will allow operation of an efficient electricity market with the participation of the private sector. Considering only the benefit of energy transmission from Guasquitas-Canjilones, the construction of the line will produce an internal rate of return (IRR) of 51%.

RISKS:

The project presents no significant risks. However, as a result of the Asian financial crisis, which prevented the offering of bonds to cover part of the financing of the Guasquitas-Canjilones plant, the IRHE recently postponed the order to begin construction of the plant. This delay could put off timely initiation of the line by reducing energy transfer during the first few years. The Government of Panama has informed the Bank of its decision to go ahead with the Estí project taking one of the following two alternatives: (a) if financing for the project comes through, the construction would be carried out under the conditions of the current contract. Upon completion, operating responsibility would then be transferred to the Estrella-Los Valles hydroelectric plant concession; or (b) the project would be incorporated within contract for the Estrella-Los Valles hydroelectric plant concession, which would include responsibility for the construction within a specified time frame. Construction would be assured in either case. To mitigate the residual risk and allow for greater flexibility, a clause has been included in the contract conditioning the call for bids on construction of the line upon the submission of satisfactory evidence by the borrower and executor that the order has been given to proceed with construction of the Guasquitas/Canjilones project, or other evidence of an energy flow sufficient to justify the line (paragraph 5.12).

THE BANK'S COUNTRY AND SECTOR STRATEGY: The current operation is consistent with the Bank's strategy because it reinforces the transmission network of Panamá and thus facilitates the operation of the private electricity market that the new privatization law seeks to establish. The loan will support the activities of the transmission company, the only operating activity that the new electricity law keeps in State hands, which will play a very important role in this reform as the enterprise charged by the law with providing nondiscriminatory open access, in technical and economic terms appropriate to the transmission network, for the generators that will compete to meet the demand. The operation fits in with the government's plans for reform of the electricity sector and thus supports the process of privatization that the government is carrying out in the sector. Finally, the operation reinforces infrastructure in Panama, one of the explicit objectives of the Bank's strategy and an essential element for supporting the development of productive private activity.

EXCEPTIONS TO BANK POLICY: Since execution of the design contract mentioned in paragraph 3.4 began in December 1996, it is requested that an exception be allowed to the Bank's policy of limiting recognition of prior expenses to those incurred within a period of 18 months before submission of the project to the Board.

PROCUREMENT OF When Bank financing is used, the minimum amounts for

GOODS AND CONTRACTING OF WORKS AND CONSULTING SERVICES:

which project procurement will be conducted through international competitive bidding will be US$300,000 for goods, US$2 million for works, and US$200,000 for consulting services. For lesser amounts, competitive bidding not restricted to the local market will be used if the amounts are greater than US$150,000 for goods, US$250,000 for works, and US$100,000 for consulting services, and a limited call for proposal or bids for amounts below these thresholds.

RECOGNITION OF PRIOR EXPENSES:

It is proposed that outlays made by IRHE for the design of the lines and substations be recognized as prior expenses, chargeable to the local counterpart funding. It is estimated that such expenses will amount to US$3.56 million.

SOCIAL AND POVERTY-RELATED POLICY CRITERIA:

The proposed program is not targeted to the poor, either geographically or in terms of beneficiaries and is not directed specifically to participation by women, as specified in the Eighth Replenishment document (AB-1704).

SPECIAL CONTRACTUAL CONDITIONS:

A. Conditions precedent to the first disbursement.

Prior to the first disbursement: (a) the government shall have signed an agreement with ETESA for the execution and transfer of resources (paragraph 4.1); (b) the legal instruments shall have been formalized for the independent operation of ETESA as the executing agency of the project, including any procedures described in paragraph 4.3 that may not as yet have been completed; and (c) ETESA shall have selected or designated an executive director for the project (paragraph 3.1).

B. Conditions precedent to the call for bids on the line and substations

Before invitations are issued to submit bids on the line, instructions shall have been given to proceed with the Guasquitas-Canjilones project or it shall have been demonstrated that there will be a supply of energy justifying the line (paragraph 5.12).

Before invitations are issued to submit bids on the construction of substations, the corresponding environmental impact assessments (EIA) shall have been approved by the IDB and the INRENARE. Also, measures in the form of technical specifications or operating and handling guidelines to mitigate these impacts shall have been developed and incorporated into the bidding documents (paragraph 3.19.c).

C. Other special contractual conditions.

Annual meetings will be held to monitor the project (paragraph 3.11). The borrower and ETESA agree that during such meetings the progress of ETESA's financial condition and its institutional situation will be reviewed and the corresponding indicators updated as indicated in paragraph 4.25.

During the first annual meeting, ETESA shall reach agreement with the Bank on an action plan to ensure that before the lines go into operation, ETESA has enough qualified staff and suitable tools and equipment to maintain the project works as well as existing ones (paragraph 3.8). Before start up of the project works and equipment, ETESA needs to adopt the preventive measures recommended in the study mentioned in paragraph 5.2.

The loan contract will also include the environmental recommendations contained in subparagraphs (a), (d), (e), and (f) of paragraph 3.19 and financial guarantees clause described in paragraph 4.21.